

It's Not Form Over Substance

Procedural Fundamentals of Making and Reviewing a Claim

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When facing a third-party claim, a policyholder and its insurer will focus significant attention on the substantive question of whether that claim is covered under the applicable insurance policies. In this article, Calfee policyholder-side coverage lawyers and Tucker Ellis carrier-side coverage lawyers have joined to discuss the procedural ins-and-outs of a coverage claim. Procedural issues are often overlooked for the substantive question of coverage, but these issues are important and can ultimately make the difference in whether a claim is covered.

How can a company be ready for a future claim by a third party?

A company waiting until a claim hits before understanding its insurance coverage program is a poor approach. A well-thought-out risk management and insurance program can mean the difference between adequate insurance protection and financial disaster. Every company should have a risk management team in place for the procurement of insurance policies and planning and managing loss-response activities.

Once insurance policies are issued and delivered, the policyholder should carefully review them to confirm the limits, terms, and provisions. Mistakes can be easily corrected by the broker and insurance underwriter shortly after issuance and before a loss occurs. After a loss, mistakes are much harder to fix.

All policies, including historical policies, must be well-organized and readily available to the risk management team. Often, decades-old policies offer significant protection against gruesome defense and indemnity costs for claims such as asbestos and environmental exposures. When facing a covered loss, a misplaced policy is the same as losing a stack of cash.

A third party makes a claim against a company. What now?

Whenever a loss or claim happens, the policyholder should review all potentially applicable policies to determine if they provide coverage. A single loss or claim may trigger a number of different policies. For example, claims that fall within the coverage of commercial general liability (CGL) policies may include allegations and claims that are also covered under Directors and Officers (D&O) policies.

After identifying the potentially applicable policies, prompt notice should be given under all of the policies. For large claims, the safest approach is to notify all primary, umbrella, and excess carriers at the same time. Depending on the circumstances, notice of a loss or claim may be given by the policyholder, its insurance broker or agent, or its outside counsel.

When should notice of a loss or claim be given to a carrier?

The importance of timing cannot be overstated. Failing to give timely notice can sometimes result in a total loss of coverage. When a loss occurs or a claim is made or reasonably anticipated, notice should be given to all relevant insurers as soon as possible. The policyholder should not make the mistake of waiting until a lawsuit is filed, because most policies consider any indication of a claim sufficient to trigger a duty to give notice. A "claim" includes things like a demand letter, or even an informal email. If a company is unsure whether something qualifies as a "claim," it should consult with outside coverage counsel.

How is notice of a claim given to a carrier?

Liability policies will typically specify the mechanics of notice: how, to whom, and

when notice must be sent, as well as what the notice should include. It is important that policyholders know, take seriously, and comply fully with these provisions.

When a third party sues a policyholder, will insurance pay for the policyholder's defense?

Many liability policies, including CGL policies, provide the insurance company with the right and duty to defend any suit seeking damages covered by the policy. Other policies, such as many D&O policies, will provide for a reimbursement of defense costs paid by a policyholder.

Even if not all claims are covered, the insurer will generally defend the whole lawsuit unless, of course, the claims are all indisputably outside the scope of coverage.

In addition, some policies provide that defense costs constitute supplementary payments that do not erode the limits of liability.

What happens after an insurer receives notice of a claim?

The insurer will analyze the applicable policy(ies) and review the claim along with any pleading that has been filed to determine if coverage exists for the claim. The insurer must respond to the notice of a claim in writing within fifteen days and commence an investigation of a claim within twenty-one days of receipt of notice. Ohio Admin. Code. 3901-1-07(C)(2), (4). In addition, the insurer must advise the insured of acceptance or rejection of the claim, or the need for more time to make such a determination, within twenty-one days after receipt by the insurer of a properly executed proof of loss. To the extent additional time is needed to assess the claim, the insurer must send the claimant an update every ninety days setting forth the need for additional time. Ohio Admin. Code. 3901-1-07(C)(12).

The carrier has multiple options for responding: (1) deny coverage; (2) defend without reserving its rights; (3) accept a defense after securing a non-waiver agreement; (4) defend under a unilateral reservation of rights; or (5) file a declaratory judgment action to determine its coverage obligations.

If the claim sets forth facts that are arguably covered under the policy, the insurer has a duty to defend the insured under Ohio law. But the insurer may accept the defense under a non-waiver agreement or a unilateral reservation of rights to preserve its coverage defenses. A reservation of rights letter provides notice that even though the insurer is agreeing to defend the policyholder at that time, some or all losses may not be covered by the terms of the policy and/or the insurer may seek reimbursement of defense costs at a later date.

What should a unilateral reservation of rights letter include?

A reservation of rights letter must (1) be timely and (2) fairly inform the policyholder of the insurer's position. To fairly inform, the insurer should identify all of the bases for a potential coverage denial under the policy, citing all relevant policy provisions and exclusions. The reservation of rights letter also should be timely supplemented as additional grounds for denial come to the insurer's attention. Failing to timely send a reservation of rights letter, update it, or fully explain the bases for the reservation of rights may result in a waiver of some of the insurer's coverage defenses.

What should a policyholder do if it receives a reservation of rights or denial letter?

A policyholder should promptly respond in writing to a reservation of rights or denial letter, setting forth all objections to the insurer's positions, and detailing why the policyholder believes coverage applies based on the pleadings, known facts, and/or policy language. The letter should also reserve the rights of the insured under the policy and applicable law.

If an insurer defends its policyholder against a third-party claim, who hires the defense counsel?

Some policies reserve the right to select defense counsel for the carrier, while other policies allow the insured to select counsel. Even when the insured is allowed to pick a lawyer, it is important to involve the carrier because often the policy will set guidelines limiting how much the insured's lawyers can be paid or requiring the selection of counsel from a specific list of lawyers known as "panel counsel." To avoid future disagreements, the policyholder and its insurer must communicate early, clearly, and regularly about these issues.

Does a policyholder have to keep its insurer updated about a loss or a claim?

Put simply, yes. Virtually all liability policies contain a cooperation clause that requires the policyholder and insurer to cooperate in the investigation, defense, and settlement of claims. The primary purposes of such clauses are to protect the insurer's ability to adjust and defend the claim and to prevent collusion between the claimant and the policyholder.

The policyholder or its lawyer should regularly send the insurer updates on litigation, including pleadings and discovery. The policyholder should also submit to interviews by defense counsel and attend depositions, court hearings, and trial as reasonably requested by the insurer.

The policyholder must notify the insurer of meaningful settlement opportunities. After all, if the insured wants the carrier to pay for the settlement, the carrier has a right to participate in the decision-making. This is not just a product of fairness; it is required by the terms of virtually every policy.

The privilege issues related to the duty to cooperate are too sticky to address substantively in this article, but it is important that policyholders and carriers consult with coverage counsel to understand the consequences before sharing privileged information.

All of these procedural hoops and hurdles make it sound like the relationship between a policyholder and its insurer is adversarial in nature. Is it?

Although policyholders and their insurers sometimes get crosswise, they fundamentally share a common goal to minimize third-party claims that one or both of them might have to pay. The procedural rules are not meant to set traps; rather, they ensure that the insureds and insurers know what to expect of each other.



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